

UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF OREGON

In Re:) Bankruptcy Case
) No. 05-64571-fra7
 RUSSELL P. ENGLE and)
 SYBIL W. ENGLE,)
) MEMORANDUM OPINION
 Debtors.)

Sewell Properties, LLC, has filed a proof of claim [No. 60] in the sum of \$76,100.00. The basis of the claim is the Debtors' personal guarantee of a lease of commercial property. The Debtors have filed an objection to the claim. The matter was heard on May 17, 2006, at Medford, Oregon. Having considered the evidence and testimony presented by the parties, I conclude that the objection to claim should be denied and the claim allowed in the amount of \$84,000.

I. FACTS

In October 2002, the claimant's predecessor in interest agreed to lease real property in Medford, Oregon to the Sybil W. Engle Trust. The lease provided for a portion of the building on the subject property, consisting of a 2,500 square foot shop and an 800 square foot office, and

1 the surrounding unpaved parking area. The lease was drawn for ten years,
2 and provided for rent of \$7,000 per month, triple net.

3 The subject properties were thereafter acquired by the
4 claimant, which succeeded as lessor. As a condition of the sale, the
5 claimant required that the Debtors personally guarantee payment of the
6 rent reserved under the lease.

7 On or about January 9, 2005, claimant was contacted by the
8 Debtors, who advised that they were closing their business. Rent
9 payments ended at that point. The Debtors surrendered possession of the
10 property on or about January 20th. The property was left in what the
11 claimant's principal described as "pretty good shape," although three to
12 four weeks were required to complete clean-up in order to re-let the
13 property. The claimant immediately entered into a listing agreement with
14 an established real estate office in Medford. The agents then undertook
15 to list the property, and show it to prospective tenants. The shop was
16 re-let in August 2005 for two years at \$2,700 per month, with an option
17 to renew.

18 Sewell Properties claims that it is entitled to the same amount
19 it would claim from the lessee itself, that is, one year's rent from the
20 date of the petition, or \$84,000. The claim is reduced by \$13,500, the
21 rent received from the new tenant. An additional claim of \$5,600 was
22 withdrawn at the hearing.

23 The Debtors argue that the claim should be denied in its
24 entirety for the reason that the claimant failed to mitigate its damages
25 as required by Oregon law. Debtors rely on Pacific General Electric v.
26 Hershiser, et al., 86 Or.Ap. 40, 738 P.2d 593 (1987) and U.S. Bank v.

1 Homeland, Inc., 291 Or. 374, 631 P.2d 761 (1981).

2 II. DISCUSSION

3 Amount of Claim

4 11 U.S.C. § 502(b)(6) provides that a lessor's claim for rent
5 is capped at the greater of (1) one year's lease payments, or (2) 15%,
6 not to exceed three years, of the remaining lease term. The cap operates
7 from the earlier of (a) "the date on which [the] lessor repossessed, or
8 the lessee surrendered, the lease property," or (b) the petition filing
9 date. A claim for any unpaid rent owing at the earlier of the two dates
10 is also retained. "This language reflects Congress' intent to limit lease
11 termination claims to prevent landlords from receiving a windfall over
12 other creditors." Sheldon H. Lolow v. PPI Enterprises, Inc. (In re PPI
13 Enterprises, Inc.), 324 F.3d 197 (3d Cir. 2003)(internal citation
14 omitted).

15 "The landlord retains a duty to mitigate the tenant's breach,
16 but any mitigation of damages secured by re-letting the premises will
17 offset only the landlord's overall potential recovery, and does not
18 affect the § 502(b)(6) cap." Id. at 208, n.17 (internal citation
19 omitted). See also Rancho Bernardo Limited Partnership v. First Alliance
20 Corp. (In re First Alliance Corp.), 140 B.R. 531 (BAP 9th Cir.

21 1992)("Post-petition payments have no relevance to a claim for rejection
22 or breach of the pre-bankruptcy lease agreement" under Code § 502(b)(6)).

23 The lessee surrendered the property to the landlord/claimant in
24 January 2005. The personal guarantee provides that the guarantee shall
25 apply for a period of two years from the effective date of the guarantee
26 (July 28, 2004). Exh. B, ¶ 6. The guarantee therefore by its own terms

1 expires on July 28, 2006. While the claim against the lessee may be for
2 unpaid rent through the end of the lease period (i.e September 30, 2012),
3 less mitigation amounts, the debtors are responsible only for the amount
4 due through July 2006: 19 months at \$7,000, or \$133,000, less any amount
5 paid in mitigation during this period. The property was re-let in August
6 2005 at \$2,700 per month, meaning that \$32,400 was paid in mitigation
7 during the period of the personal guarantee (12 x \$2,700). The total
8 claim against Debtors is therefore \$100,600 (\$133,000 - \$32,400), limited
9 by § 502(b)(6) to \$84,000 (12 x \$7000).

10 Mitigation of Damages

11 Debtors argue that the claim should be denied because the
12 claimant failed to mitigate its damages. The Oregon Supreme Court held
13 in United States National Bank of Oregon v. Homeland, Inc. at 380-381
14 that, while a "lessor has a duty to make a reasonable effort to mitigate
15 damages by finding a suitable tenant," . . . the "mere acceptance and re-
16 letting of the surrendered premises does not release the tenant from
17 contractual liability for breach of contract." The Oregon Court of
18 Appeals elaborated on this by holding that "the lessor not only has a
19 duty to mitigate, it also has the burden to prove that it made a
20 reasonable effort to find a suitable tenant" Portland General
21 Electric v. Hershiser et al. at 44.

22 I find, based on the evidence and testimony presented, that the
23 claimant has met its burden to prove that it made a reasonable effort to
24 mitigate damages. It immediately entered into an agreement with an
25 established real estate firm which undertook to list the property and
26 show it to prospective tenants. While no evidence was presented as to

1 fair market rental value of the property, one can assume that the real
2 estate firm and the lessor, absent evidence to the contrary, sought the
3 terms most advantageous to the lessor. The claimant acted reasonably and
4 expeditiously in mitigating its damages.

5 III. CONCLUSION

6 Code § 502(b) provides that if an objection to a claim is made,
7 the court shall determine the amount of such claim as of the bankruptcy
8 filing date. For the foregoing reasons, I find that the claim should be
9 allowed in the amount of \$84,000. An order to that effect will be
10 entered.

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13 FRANK R. ALLEY, III
14 Bankruptcy Judge
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